Despite a looming political crisis, Greece is no longer the threat to the Eurozone that it was in 2012

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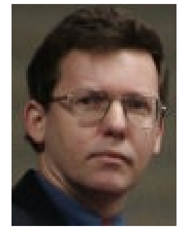
The Greek parliament is due to hold a second round of voting on 23 December to elect the country's next president, following an unsuccessful vote last week. **Remy Davison** *writes that while the threat of a political crisis is very real, the situation is very different from 2012, where the country's economic problems threatened to spill over into a wider Eurozone crisis.*



Markets loathe uncertainty. They particularly despise uncertainty as the year draws to a close. No trader wants to devote the Christmas-New Year shutdown to biting their finger nails, having gone stupidly long on Greek bonds. On 13 December, all of the major European market indices fell, victims of the general air of pessimism about 2015. Fortunately, on 18 December, Euro markets rallied in their biggest gain in three years as Greek opposition leader, Alexis Tsipras, committed to keeping Athens in the Eurozone.

But the parliamentary crisis brewing in Greece still has the potential to spill over into the brittle Eurozone economy. Greek legislators held an inconclusive first-round vote for a new president on 17 December. A second round will be held on 23 December, while a third round, if required, will take place on 29 December. However, Greek Prime Minister Antonis Samaras' coalition government may not command enough votes to elect Stavros Dimas, Samaras' preferred candidate. If the Greek parliament fails to elect a new head of state, this automatically paves the way for a snap parliamentary election, with Tsipras' Coalition of the Radical Left (Syriza) currently leading the opinion polls.

Samaras is playing a dangerous game. On the one hand, he is counting on Greek voters' support for a 'clean exit' from the 2011 bailout, meaning an end to budgetary monitoring imposed by the troika: the European Commission, IMF, and European Central Bank. Samaras is conjuring up a future where there is no requirement for an EU line of credit, coupled with a cautious restoration of Greek fiscal sovereignty. However, markets have already denied him his clean break. The IMF programme for Greece is scheduled to run until 2016, which means it will continue to monitor the Greek government's adherence to conditionality.

On the other hand, the Prime Minister portrays Syriza and Tspiras as potential wrecking balls who would squander the hard-won gains of the past two years. But unless Samaras can convince 180 parliamentarians to elect Dimas in the third round on 29 December, a snap election is likely to be held, with Syriza odds-on to win the most seats in the next parliament.

Austerity: the key to Syriza's rise

During the second 2012 election campaign, when Syriza's emergence as the largest parliamentary grouping looked possible, Tsipras played the role of the radical. He travelled to Berlin to meet with German Left counterpart, Oskar Lafontaine, and press for an end to austerity in Greece. He warned of "world war" if Europe plunged into economic crisis. Both Angela Merkel and François Hollande refused to meet with Tsipras.

Tsipras played fast and loose in the 2012 elections. He described the harsh medicine imposed upon Greece by Berlin as "brutal." He refused to join a unity coalition led by Samaras' conservatives, labelling Samaras the "Prime Minister of chaos", and New Democracy's acquiescence to the bailout as " criminal". He drew plaudits and popular support for demanding an end to the EU/IMF bailout and a moratorium on Greek debt; and he called Merkel's bluff, arguing that the EU would not risk Greece's expulsion from the Eurozone, while Greece would never leave willingly.

Since the 2012 crisis, Syriza and Tsipras have travelled their own road to Damascus. Quietly, their demands have moderated, although the anti-austerity message remains front and centre. Tspiras has canvassed modest reforms, such as tackling tax evasion and loans to establish a job creation programme. However, none of these measures would have a substantial, positive impact upon either public revenues or Greek unemployment, which is still over 25 per cent.

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Syriza's answer to the crisis is to demolish key elements of the austerity regime, such as reversing the pension and wage cuts in an attempt to boost domestic demand. Tsipras also plans to end privatisation and labour market reforms. But the centrepiece of Tsipras' programme is to withdraw from the bailout conditions. Since 2011, the EU and IMF have advanced over €240 billion in loans to Greece, recapitalising the country's banks, but also repaying excessively-leveraged French and German banks, which hold the largest tranches of Greek debt.

Yanis Varoufakis, an academic economist who is expected to play a key advisory role in the event of a Tsipras government, argued recently that "Greece cannot stand up on its feet as long as its debt remains un-payable, its banks insolvent and its private sector incapable of repaying its taxes, debts and wages".Varoufakis is right to label the problem a systemic crisis within the Eurozone, which has culminated in a "triple crisis" in Greece, comprising insolvent banks, insurmountable debt and a moribund private sector. The 'pauperisation' of Greece is readily apparent. So, what is to be done?

As long as the fiscal strictures upon Greece bind governments to surpluses of around 4.5 per cent of GDP, Athens has virtually no room for manoeuvre. At best, what is needed is debt forgiveness and restructuring, albeit under EU institutional supervision, in order to reflate the Greek economy. A sub-optimal solution would be a debt pause, allowing the Greek economy time to recover and grow (no mean feat in a flat European economy).

The alternative is the rise of extremism on the EU's Mediterranean periphery, a disillusioned population and an exodus of young people, for whom Greece no longer represents a viable financial future. The extinction of Greek fiscal sovereignty has produced a prolonged recession, alarming unemployment, riots and government asset firesales. Despite this, Athens has performed a creditable and credible economic turnaround in the last two years, albeit at an extremely heavy social cost. Credit markets rewarded Samaras' punishing prescriptions with an oversubscribed bond auction in April.

Greece's credit rating is still in the gutter, but a debt pause or forgiveness may return some investor confidence to the country. True, European creditors would need to absorb the costs, having already taken a haircut in 2012. But it serves no financial or public good to saddle Athens with unpayable debts. As a number of economists have argued previously, even maturity extensions to IMF loans and ECB repurchasing of sovereign bonds would not make Greece solvent. Consequently, more robust solutions, such as debt forgiveness, need to be developed by Eurozone members.

The global economy of 2014 is a different animal from that of 2012. Greece alone cannot bring down the Eurozone. In 2012, it was a fear of contagion and, more ominously, the prospect of one of Europe's larger economies – Spain or Italy – falling victim to the sovereign debt crisis. The EU's fiscal and financial stabilisation instruments were severely lacking two years ago, leading Mario Draghi to declare the ECB would do "whatever it takes" to save the Eurozone.

However, although the Eurozone is by no means impervious to shocks, and remains stubbornly impervious to growth, the financial architecture of Europe appears much more reassuring to markets and credit agencies alike. In other words, progressive reform in a period of relative stability is vastly preferable to the muddled, crisis politics that characterised Eurozone decision making in 2012.

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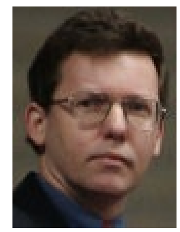
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